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DEPARTMENT OF TRANSPORTATION
WASHINGTON, D.C.

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Joint Application of

UNITED AIR LINES, INC.

and

DEUTSCHE LUFTHANSA, A.G.

(LUFTHANSA GERMAN AIRLINES)

under 49 U.S.C. 41308 and 41309 for
approval of and antitrust immunity for
an expanded alliance agreement

Docket OST 96-1116 -15

JOINT REPLY OF UNITED AIR LINES, INC.
AND DEUTSCHE LUFTHANSA, A.G. (LUFTHANSA GERMAN AIRLINES)

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United Air Lines, Inc. ("United") and Deutsche Lufthansa A.G. ("Lufthansa") hereby reply to the Answers filed in the instant docket on April 3, 1996.

Introduction

Six Answers were filed in response to the Joint Application ("Application"). One, filed by the City and County of Denver, supports the Application, citing the additional benefits that would accrue to Denver from the expanded United/Lufthansa alliance. Another, filed by the International Air Transport Association ("IATA"), takes no position on the Application but urges the Department to refrain from considering the issue of IATA tariff coordination in this proceeding. Three Answers, filed by American Airlines, Inc. ("American"), Delta Air Lines, Inc. ("Delta"), and Northwest Airlines, Inc. ("Northwest"), while taking no position on the merits of the

Application, urge that immunity be granted only under certain conditions. A sixth Answer, filed by Trans World Airlines, Inc. ("TWA"), opposes the Application.

The Applicants agree with the points raised in the Denver and IATA Answers: Denver and cities like Denver will enjoy significant benefits from the Alliance Expansion Agreement between United and Lufthansa; and IATA tariff coordination is not an issue that can be appropriately or fairly addressed in the context of this proceeding. The remainder of the Joint Reply is devoted to the Answers filed by American, Delta, Northwest and TWA.

The carriers' Answers raise five discrete matters:

(1) whether the Department should act upon the Application before acting upon antitrust immunity applications filed by Delta and its European air carrier partners, and American and Canadian Airlines International; (2) whether the Alliance Expansion Agreement satisfies the Clayton Act merger standards; (3) the willingness of German tour companies and charter airlines to participate in SABRE and the extent of Lufthansa's participation in SABRE and WORLDSPAN; (4) the future availability of slots at German airports; and (5) a provision in the Alliance Expansion Agreement requiring the parties to discuss with each other possible code sharing arrangements with third parties. Each of these five matters will be addressed in turn.

I. THE TIMING OF THE DEPARTMENT'S RULING ON THE INSTANT APPLICATION IS UNAFFECTED BY THE PENDENCY OF THE OTHER APPLICATIONS CONCERNING DIFFERENT ALLIANCES.

With the filing of the instant reply, the record before the Department is complete and the Application ripe for decision. The record clearly demonstrates that numerous benefits would accrue from a Department decision approving and granting antitrust immunity to the Alliance Expansion Agreement. As detailed in the Application, it would enable United and Lufthansa to increase significantly the integration of their global route networks, increase the availability of seamless online services, achieve economies of scale, lower costs and increase competition in the global marketplace. Moreover, it would bring into full force the Open Skies Agreement recently concluded between the United States and Germany.

While not disputing any of these benefits, American and Delta urge the Department not to act on the instant Application until it has granted antitrust immunity for their respective alliance agreements." Neither American nor Delta has provided any valid justification for delaying action on the Application.

It is clearly established that a federal agency may control its own calendar subject, of course, to due process or statutory considerations.² "[T]he subordinate questions of

^{1/} American makes this request expressly (see American Answer at 2: "United and Lufthansa should be required to wait their turn"); Delta implicitly asks for the same preferred treatment when it demands the "highest priority" for approval of its alliance (Delta Answer at 2).

^{2/} See City of San Antonio v. CAB, 374 F.2d 326, 329 (D.C. Cir. 1967) ("No principle of administrative law is more firmly established than that of agency control of its own calendar.") While the Department is required to act upon Delta's and American's applications "within a reasonable time" as required by the

procedure . . . -- the scope of the inquiry, whether applications should be heard contemporaneously or successively, whether parties should be allowed to intervene in one another's proceedings, and similar questions -- were explicitly and by implication left to [the federal agency's] own devising [so long as due process requirements are observed]." F.C.C. v. Pottsville Broadcastins Co., 309 U.S. 134, 138 (1940).

Although American and Delta advance arguments why their own applications should be approved "fairly and expeditiously," Delta Answer at 2, neither alleges any facts suggesting that the carriers' due process rights or any applicable statutory provision requires the Department to delay acting on the Application. Clearly, therefore, the Department is free to decide the instant Application once it is clear -- as it now is -- that the United-Lufthansa Alliance Expansion Agreement satisfies the requirements of 49 U.S.C. §§ 41308 and 41309. Prompt action on the Application is plainly in the public interest, without regard to the timing of the Department's review of the Delta and American applications."

Administrative Procedure Act, 5 U.S.C. §555(b) (1995), this bears no relationship to the speed with which it should act on the instant Application.

^{3/} The Department's discretion to move forward now with the instant Application is confirmed by the material factual differences among the three applications. For example, American and Canadian are seeking immunity for a transborder alliance even though entry by U.S. carriers into transborder city pairs involving Canada's three largest cities, which account for the lion's **share** of transborder traffic, remains subject to significant limitations until early next year in the **case** of Montreal and Vancouver and until early in 1998 in the case of Toronto. No such limitations

II. THE ALLIANCE EXPANSION AGREEMENT CLEARLY SATISFIES THE CLAYTON ACT STANDARDS AS APPLIED BY THE DEPARTMENT.

In determining whether agreements such as the Alliance Expansion Agreement are consistent with the antitrust laws, the Department applies the standard Clayton Act test used in evaluating whether mergers will likely reduce competition substantially in any relevant market.'" Joint Application of Northwest Airlines, Inc. and KLM Royal Dutch Airlines, Order 92-11-27 at 13. "The Clayton Act test requires us to consider whether the Agreement will substantially reduce competition by eliminating actual or potential competition . . . so that [the carriers] would be able to raise prices or reduce service below competitive levels." Id.

TWA argues that the Alliance Expansion Agreement fails to satisfy this test. TWA Answer at 4. Its argument relies largely on HHI calculations generated by it for what it describes as the U.S.-Germany market.'" TWA contends that these

exist in the Open Skies agreement concluded between the United States and Germany.

^{4/} TWA suggests in passing that the instant application should not be judged as if it were a merger under Section 7 of the Clayton Act because there is "no evidence that these carriers would merge if they could." TWA Answer at 4. In KLM/Northwest, the Department decided to apply the Clayton Act standard to the Commercial Cooperation and Integration Agreement between KLM and Northwest based on the fact that "Northwest and KLM represent that the Agreement is intended to integrate the two carriers' operations so that they will operate as a single carrier." Order 92-11-27 at 13. Lufthansa and United have made the same representation in their Joint Application. See Joint Application at 9, 13, 27-28.

^{5/} See TWA Answer at 5 ("TWA's HHI calculations show that this agreement would not be approved if it involved a merger of the two applicants.") TWA also contends in a paragraph that the

calculations demonstrate that a United-Lufthansa merger would impermissibly increase concentration in a U.S.-Germany market, permitting Lufthansa and United to exercise market power to the detriment of passengers. TWA further contends that potential competition will not restrain the exercise of market power, because barriers to entry preclude entry or expansion of service between the United States and Germany. TWA's argument is fatally flawed.

A. TWA's HHI calculations based on the number of seats offered on nonstop sectors between the U.S. and Germany substantially overstate concentration in the market for air transportation between the United States and Germany.

TWA's HHI calculations substantially overstate concentration in the market for air transportation services between the United States and Germany for two reasons. First, TWA attempts to gauge market concentration by looking only at the number of seats available on nonstop flights between the United States and Germany. The HHIs calculated from these numbers fail to account for U.S.-Germany passengers transported over non-German and non-U.S. hubs. They also ignore the fact that a significant percentage of the capacity available on United's and Lufthansa's nonstop U.S. -Germany flights is utilized by

United-Lufthansa Alliance Expansion Agreement "will eliminate the threat of potential competition" in several city pairs. TWA Answer at 8. However, TWA makes no attempt whatsoever to satisfy, and indeed is unable to satisfy, the rigorous requirements for proving an "actual potential competition" claim under Section 7 of the Clayton Act. See, e.g., BAT Industries Ltd., 104 F.T.C. 852 (1984).

passengers who originate in or are destined for a third-country point beyond or behind Germany or the United States.

Second and most importantly, in calculating market shares, TWA fails to include carriers offering U.S.-Europe services that would be made available to greater numbers of U.S.-Germany passengers if United and Lufthansa attempted to raise prices above, or reduce output below, competitive levels.

1. TWA's HHI calculations are distorted by their failure to account properly for connecting passengers.

TWA acknowledges that its HHI calculations exclude passengers travelling between the United States and Germany who connect over points outside Germany and the United States. TWA attempts to minimize the seriousness of this failing by arguing that "except possibly for British Airways, it is unlikely that any third country carrier achieves more than a 1% market share of U.S.-German traffic" (TWA Answer at 6-7) and that, in any event, connecting service is never a substitute for nonstop service. Id. at 7.

In fact, the competitive significance of such third-country carriers transporting U.S. -Germany passengers over non-German and non-U.S. hubs is considerably greater than TWA suggests. The information available to Lufthansa suggests that perhaps one-sixth of all passengers travelling between the United States and Germany are transported by third-country carriers over a non-German European hub such as London, Amsterdam, Brussels,

Copenhagen or Luxembourg. Indeed, from some important Germany cities, the third-country carrier share of traffic to the U.S. exceeds 25%. Moreover, this share would appear to **be** increasing. For example, British Airways has stated publicly that "the number of passengers flying from Germany to London and then to North America has increased by more than 10 percent over the past year" and that it expects additional growth this year.^{6/} Thus, contrary to TWA's unsubstantiated claim, its exclusion of third-country carrier connecting service significantly distorts its HHI calculations.

A second serious shortcoming of TWA's HHI calculations relating to "connecting service" -- one that TWA does not address -- is that they improperly include the large number of seats on Lufthansa and United nonstop U.S.-Germany flights that are occupied by passengers originating in or destined for third-country points behind or beyond Germany or the United States. In Lufthansa's case, Frankfurt has become a major connecting point for transatlantic passengers originating in or destined for points in Eastern Europe, the Middle East, the Indian subcontinent, and Africa.^{7/} In United's case, its Chicago-Frankfurt and Washington-Frankfurt nonstop services serve as a vital bridge between United's route networks in Asia the South

^{6/} Michael Skapinker, "BA Attacks U.S.-German Antitrust Move," Financial Times, March 6, 1996, p.4.

^{7/} Indeed, elsewhere in its Answer, TWA recognizes as much: "At Frankfurt, a significant portion of the traffic carried on transatlantic service is Sixth Freedom traffic, originating and or destined to points behind the gateway." TWA Answer at 11.

Pacific, Latin America and domestically in the United States, on the one hand, and the points to which it code shares with Lufthansa beyond Frankfurt, on the other. Under these circumstances, no reliance can be placed on an HHI calculation that treats every Lufthansa and United nonstop U.S.-Germany flight as carrying only passengers originating in Germany and destined for the U.S., or vice versa. That is not the reality of Lufthansa's or United's passenger mix.

2. TWA's HHI calculations fail to include the U.S.-Europe services that would, automatically and with little or no sunk cost, begin to transport more U.S.-Germany traffic if United and Lufthansa attempted to raise prices or restrict output.

Obviously, HHI calculations based on wrongly defined markets are useless.^{8/} That is the problem with TWA's HHI calculations: they are premised on a fundamentally erroneous definition of the U.S.-Germany market.

The "U.S.-Germany market" is shorthand for the multitude of U.S. and German city pairs that taken as a whole constitute the universe of possible air travel routes between origins and destinations in the two countries. Nonstop service is available between only a very small number of these city-

^{8/} "In order to analyze whether the statistical evidence of market concentration resulting from a particular proposed merger establishes a presumption that the merger may substantially lessen competition in violation of the Clayton Act, the relevant product and geographic markets in which competition may be affected must be defined." California v. American Stores Co., 697 F. Supp. 1125, 1129 (C.D.Cal. 1988), aff'd in relevant part, 872 F.2d 837 (9th Cir. 1989), reversed on other grounds, 493 U.S. 915 (1989).

pairs; travel between the vast majority of U.S.-Germany city-pairs involves one or more changes of airplanes, occurring in the United States, Canada, Western Europe or Germany.

In arriving at its HHI calculations for the U.S.-Germany market, however, TWA has included only the seats of those carriers offering nonstop U.S.-Germany service; it has thereby failed to include numerous U.S. and foreign carriers that currently make seats available to passengers travelling between the United States and Germany and would make additional seats available to such passengers if a profit opportunity existed.

Take as a hypothetical example a passenger seeking to travel from New Orleans to Hamburg. All else being equal, this passenger might choose to fly United and Lufthansa on a New Orleans-Washington-Frankfurt-Hamburg routing. If United and Lufthansa were to attempt to raise fares or restrict service on this route, however, the passenger could travel just as easily over a New Orleans-Philadelphia-London-Hamburg routing utilizing USAir and British Airways, or a New Orleans-Atlanta-Brussels-Hamburg routing utilizing Delta and Sabena, or any one of the dozens of other available routings involving two changes of plane.

Any attempt by United and Lufthansa to raise prices or restrict output with respect to their U.S.-Germany services would be met by the supply responses of other firms -- U.S. and third country carriers offering a myriad of online or interline change-of-aircraft services between the U.S. and Germany. These

responses would occur as carriers redirected capacity on existing services to the higher yielding U.S.-Germany traffic. The redirection would occur automatically, as yield management systems targeted higher yielding traffic, and with little or no sunk costs, as the carriers would already be operating aircraft over the routes.

The Merger Guidelines specifically require that such firms be considered as market participants:

[T]he Agency will identify other firms not currently producing or selling the relevant product in the relevant area as participating in the relevant market if their inclusion would more accurately reflect probable supply responses. These firms are "uncommitted entrants." These supply responses must be likely to occur within one year and without the expenditure of significant sunk costs of entry and exit, in response to a "small but significant nontransitory price increase."

Department of Justice and Federal Trade Commission Horizontal Merger Guidelines, § 1.32.

In light of the existence of bountiful "uncommitted entrants" which could easily expand their capacity in the market for air transportation between the U.S. and Germany, the degree of competitiveness in the U.S.-Germany market is better indicated by the HHI calculations for the U.S.-Europe market presented in the Application. See Application at 30. Virtually all carriers offering U.S.-Europe service are effectively "uncommitted entrants" in the U.S.-Germany market. In any event, the HHI figures proffered by TWA, based on an incomplete description of the relevant market, are in no way probative of TWA's claim that

the United-Lufthansa Alliance Expansion Agreement would increase concentration and lessen competition in U.S.-Germany air transportation.

B. Allegations of barriers to entry are at odds with recent carrier entry and expansion in the U.S.-Germany market, and inconsistent with the Department's international aviation policy.

TWA alleges that, notwithstanding the removal of frequency caps under Open Skies, "significant barriers to entry" effectively preclude entry or expansion in the U.S.-Germany market and thus that the threat of potential competition will not prevent United and Lufthansa from exercising market power. TWA Answer at 8-11. As discussed above, United and Lufthansa will have no market power in the U.S. -Germany market and TWA's woefully wrong HHI calculations do not demonstrate otherwise. Moreover, the allegation that significant barriers preclude entry or expansion in the U.S.-Germany market is at odds with recent experience and is inconsistent with the carefully considered premises of the Department's international aviation policy.

1. TWA's claim that new U.S.-Germany services cannot be successfully launched is contradicted by ample recent evidence.

Contrary to TWA's contention, carriers have not been precluded from entering and operating successfully in the U.S.-Germany market. Currently, six U.S. carriers and five third-country carriers offer scheduled nonstop services between the

United States and Germany." One new carrier, **and several new** services, are scheduled to enter the market this summer season.^{10/} By this summer, one carrier -- USAir -- will have commenced three new nonstop U.S.-Germany services in the last year alone.^{11/} Such evidence demonstrates that carriers can effectively enter and expand in U.S. -Germany markets and wholly undermines TWA's contrary contention.

2. TWA's claim that new U.S.-Germany services cannot be successfully launched is inconsistent with the marketplace realities underlying the Department's international aviation policies.

TWA's argument that new entry will not occur in the U.S.-German market under the Open Skies regime is starkly at odds with a fundamental tenet of the Department's international aviation policy, namely, that Open Skies agreements can be expected to lead to an increase in the services available to consumers. This premise was clearly articulated in the

^{2/} It should be noted that this is a far larger number of carriers than were present in the U.S.-Netherlands market when KLM and Northwest were granted immunity. See Application at 31-32.

^{10/} Pursuant to the Memorandum of Consultations concluded between the United States and Germany, all U.S. carrier applications for third- and fourth-freedom frequencies filed in Docket OST-95-813 will be granted. Accordingly, new services by Continental, USAir, World, Delta, and United will be commenced shortly. Moreover, since these applications were granted, Continental has announced its intention to start new Newark-Dusseldorf service this summer. See Aviation Daily, April 12, 1996 at 80.

^{11/} USAir commenced Boston-Frankfurt and Philadelphia-Frankfurt services in 1995, and plans to commence Philadelphia-Munich services this summer.

Department's decision to grant antitrust immunity to the KLM/Northwest agreement. In that proceeding, the Department noted that "even if a merger creates a firm with a dominant market share, the merger would not substantially reduce competition if other firms have the ability to enter the market within a reasonable time if the merged firms charge supra-competitive prices." Order 93-11-27 at 15. Stating that "[a]s a result [of the Open Skies Agreement], other carriers have the opportunity and ability to enter the U.S.-Netherlands market and to increase their service," *id.* at 15-16, the Department concluded that the proposed integration would not permit the applicants to charge supra-competitive prices or reduce service below competitive levels.^{12/}

The Department's position that the elimination of capacity and frequency controls will generate new entry and expansion is amply supported by the history of deregulation of the United States' domestic aviation market.^{13/} It is also supported in the instant case by the inescapable fact that there will be more U.S. carrier services in the U.S.-Germany market

^{12/} Under the U.S.-German Open Skies Agreement, carriers will have the same opportunity and ability to enter the U.S.-Germany market, which will have the same effect of precluding supra-competitive prices or reductions in service below competitive levels. *See* "U.S., Germany Reach "Open Skies" Aviation Agreement," Department of Transportation Press Release, Feb. 29, 1996 (quoting Secretary Peña: "This [Open Skies] agreement can dramatically expand service and price options for consumers of both nations.") .

^{13/} *See, e.g.,* Report of Secretary's Task Force on Competition in the U.S. Domestic Airline Industry (February 1990) at 1.

this summer because frequency caps have been lifted than there would have been if the caps had remained in place.

III. THE CRS CLAIMS OF AMERICAN AND TWA ARE IRRELEVANT AND UNTRUE.

American and TWA argue that the Department's approval of the Application should be conditioned on (i) changes in the CRS affiliations of certain German tour companies and German charter airlines, and (ii) expanded Lufthansa participation in SABRE, the CRS system affiliated with American, and in a new "enhanced CRS product" offered by WORLDSPAN, the CRS system affiliated with TWA. American Answer at 3-7; TWA Answer at 12-13.

None of these CRS issues is relevant to the issue before the Department -- namely, whether the instant Application satisfies the statutory standard for approval and antitrust immunity for an international air carrier alliance. While both American and TWA suggest that these CRS changes are necessary for carriers to compete against United and Lufthansa in the U.S.-Germany market, neither explains why this is so or even suggests that their own U.S.-Germany air travel services are not adequately and fairly distributed through the various CRS systems available in Europe, including Amadeus. Nor can there be any contention that CRS competition would somehow be affected by the Alliance Expansion Agreement: the Agreement explicitly excludes from the activities the parties intend to coordinate the

management of United's and Lufthansa's interests in CRS systems.^{14/}

Upon any fair examination, it is clear **that these** irrelevant CRS issues are merely attempts by American and TWA to extract from Lufthansa (i) guarantees regarding the future actions of independent entities over which Lufthansa has no control, and (ii) commercial concessions, unrelated to American's and TWA's U.S.-Germany services, designed to obtain advantages for SABRE and WORLDSPAN in the CRS business -- a distinct industry in which SABRE, WORLDSPAN, Amadeus, and Galileo compete intensely.

A. Lufthansa has no control over the CRS affiliations of German tour companies and charter carriers.

American complains that several major tour companies and charter carriers in Germany do not participate in SABRE, opting instead to participate in Amadeus, a CRS system in which Lufthansa owns a 29% share (the other shareholders are Continental Airlines, Air France, and Iberia). Although American alleges darkly that "[t]hrough cross-ownership and other affiliations, Lufthansa has orchestrated a concerted effort that has had the effect of keeping the largest tour companies out of SABRE, and of minimizing participation in SABRE by German charter carriers," American offers no credible evidence that Lufthansa

^{14/} See Alliance Expansion Agreement, Article 4.10.

has -- or could have -- controlled the CRS decisions of these tour companies and charter carriers.

In fact, Lufthansa has orchestrated no such effort and exercises no control over the CRS decisions of these companies. The two German charter carriers whose decision not to participate in SABRE American seeks to ascribe to Lufthansa -- Hapag-Lloyd and Eurowings -- are in no way under Lufthansa controls'; in fact, both compete with Lufthansa. Indeed, the only charter carrier that Lufthansa does control, Condor, participates in both SABRE and WORLDSPAN on the same basis that it participates in Amadeus.

Nor does Lufthansa direct the CRS decisions of any of the German tour companies American names. While American is particularly aggrieved by its inability to secure the participation of TUI in SABRE, it offers no evidence that TUI, an independent company, takes directions from Lufthansa. In fact, the news report that American attaches to its Answer indicates that Lufthansa and TUI are distinct commercial entities that have engaged in "tough rounds of discussions", and that, in utilizing CRS services, TUI acted in a manner consistent with its own interest as a shareholder of START.

^{15/} Lufthansa has an 18% minority ownership stake in Hapag-Lloyd, and no stake at all in Eurowings. It controls neither of these carriers.

**B. Lufthansa participates fully in SABRE and
WORLDSPAN.**

While American and TWA acknowledge that Lufthansa participates in SABRE and WORLDSPAN, both fault the degree of "functionality" through which Lufthansa services are offered on those networks. American contends that Lufthansa has failed to provide certain functions such as seating preferences, wait list priority, class of service upgrades, ticketless transactions and tickets on departure (in Germany) through the SABRE system. American Answer at 6-7. TWA complains that Lufthansa has "been slow to participate in WORLDSPAN enhanced products, such as WorldGroup." TWA Answer at 13.

Neither American nor TWA suggests how SABRE's and WORLDSPAN's ability to market Lufthansa's services bears in any way on the abilities of American, TWA and other carriers to compete with United and Lufthansa in any U.S.-Germany market. If anything, reduced functionality for distribution of Lufthansa would seem to benefit the competitive position of American and TWA as air carriers, whatever effect it might allegedly have on their affiliated CRS systems.

In any event, the allegations of both carriers are false. Lufthansa makes available to SABRE the highest degree of functionality that it makes available to any CRS, including Amadeus. (While SABRE may be dissatisfied with certain limitations on the functions made available by Lufthansa, these limitations are encountered by every other CRS, including Amadeus.) Moreover, Lufthansa would note that it has continued

to maintain this high functionality, notwithstanding the fact that it has encountered numerous difficulties with respect to overcharging by SABRE. With regard to TWA's complaint, Lufthansa has sought repeatedly to expand its participation in WORLDSPAN, but has been stymied by WORLDSPAN's unwillingness to accommodate certain Lufthansa requirements such as numeric availability status messages (NAVF), real time updating of schedules (SSIM), and point-of-sale or point-of-booking control.

Finally, to the extent that American or TWA seriously wish to pursue CRS issues, other proceedings and other forums -- under U.S. law, EU law, or German law -- are available and far better suited to address their concerns. See, e.g., American Answer at 5 n.3. There is absolutely no reason to drag these wholly irrelevant issues into this proceeding.

IV. THE DEPARTMENT DOES NOT NEED TO ADDRESS **ANY** ISSUE
CONCERNING FRANKFURT SLOTS.

Northwest urges that the Department "insure the availability of slots for U.S. carriers at Frankfurt International Airport in the context of considering this application." Northwest answer at 1. TWA contends that "Lufthansa should be required to make slots available, at the time requested, to U.S. flag carriers desiring to enter the U.S.-Germany market or to expand service." TWA goes on to suggest, after noting that the head of the coordinating committee is an individual employee of Lufthansa, that "[u]nder these circumstances, Lufthansa should be the guarantor of entry by U.S.

carriers if it receives antitrust immunity." TWA Answer at 14-15.

Neither TWA nor Northwest contends that it has been denied a slot for a service that it has sought to commence or expand at Frankfurt or any other German airport. Indeed, Northwest concedes that it has the airport slots it requires in Germany at the present time. Although Frankfurt is subject to slot coordination, which affects Lufthansa more than any other carrier, the applicants believe that there is scope for significant expansion of commercially viable U.S. carrier services at Frankfurt and at other German airports.

TWA's suggestion that Lufthansa should be made to act as "guarantor" for slot availability to U.S. carriers reflects a fundamental misunderstanding of the legal status of slot allocation at German airports. As indicated in the Application, slot allocation is conducted according to Council Regulation 95/93, a European Union regulation that prescribes mandatory rules for slot allocation at congested airports throughout the European Union. Under this Regulation, Lufthansa is not allowed to transfer its slots to another carrier. Instead, any slots that Lufthansa does not use must be put in a pool for allocation by an independent coordinator, who is appointed by the Federal Minister for Transport.

Under Regulation 95/93, the coordinator is legally obliged to act "in a neutral, non-discriminatory and transparent way". Furthermore, Regulation 95/93 obliges Germany, as it does

other EU Member States, to ensure that the coordinator "carries out his duties in an independent manner." It may be noted that the "Coordinating Committee" to which TWA refers does not itself allocate slots, but rather acts in an advisory capacity. The coordinating committee is chaired by a representative of the Transport Ministry and includes delegates from the Federal States and the air traffic control authority, airline and airport representatives, as well as the Coordinator.

The current coordinator and a number of his staff retain a purely technical employee relationship with Lufthansa solely to retain certain pension rights and other benefits under German law. This status reflects the fact that, prior to 1993, slot allocation was conducted by the airlines through IATA. The German government has deemed it appropriate to take advantage of the experience of the people who ran the allocation process under IATA in the new regulatory system. Allowing the persons involved to retain airline employee status preserved pension rights and other fringe benefits that would otherwise have been limited or lost. The salaries of these persons are not paid by Lufthansa, however, but rather by an association of all German airspace users. Most important, the coordinator and his staff are not subject to direction by Lufthansa. They are instead subject to the direction and disciplinary powers of the Transport Ministry. TWA's suggestion that Lufthansa could preclude U.S. carriers from initiating or expanding U.S. -Germany services by controlling the slot allocation process is thus patently false.

V. SECTION 6.2 OF THE ALLIANCE EXPANSION AGREEMENT SHOULD NOT BE EXCLUDED FROM THE GRANT OF ANTITRUST IMMUNITY.

TWA contends that antitrust immunity should be conditioned on elimination of Article 6.2 of the Alliance Expansion Agreement which, TWA alleges, "locks the parties into each other, and eliminates, as a practical matter, the potential for any other carrier to code share in the U.S.-Germany market with either United or Lufthansa." TWA Answer at 14.

Article 6.2 of the Alliance Expansion Agreement states:

Alliances With Other Carriers. Each Party shall notify in advance and discuss with the other Party, in the manner contemplated in Article 2.11 of the 1993 Agreement, any Cooperative Agreement which it proposes to enter into with any third party Air Carrier, or any significant extension or amendment which it proposes to make to any existing Cooperative Agreement with any third party Air Carrier, following the Effective Date. In order to maximize synergies and enhance customer service, the Parties shall seek to have alliances with the same third party Air Carriers, where feasible.

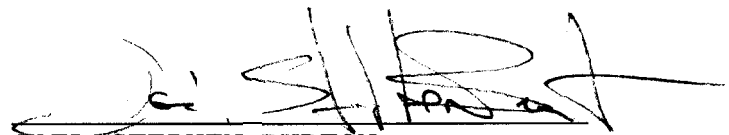
Contrary to TWA's contention, Article 6.2 plainly does not "eliminate the potential" for either Party to enter into a separate code share arrangement with another carrier between the United States and Germany. Indeed, United currently code shares with British Midland on London-Frankfurt services for connecting U.S.-Germany traffic flows. Article 6.2 merely requires, reasonably enough, that each party "notify in advance and discuss with the other party" any such relationship.

Conclusion

In light of the foregoing, United and Lufthansa renew their request that the Department approve the Alliance Expansion

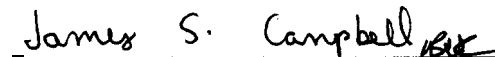
Agreement under 49 U.S.C. 41309 and exempt United and Lufthansa and their respective affiliates from the antitrust laws pursuant to 49 U.S.C. 41308, for a period of no less than five years in duration, to allow the applicants to proceed with the Alliance Expansion Agreement.

Respectfully submitted,



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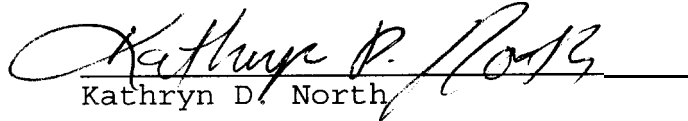
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DATED: April 12, 1996
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CERTIFICATE OF SERVICE

I hereby certify that I have this date served a copy of the foregoing Joint Reply of United Air Lines, Inc. And Deutsche Lufthansa, A.G. (Lufthansa German Airlines) on all persons named on the attached service list by causing a copy to be sent via first class mail, postage prepaid.


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